No. 82-1571

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

FIRST ALABAMA BANK OF MONTGOMERY, N.A.
Petitioner,

v.

CHARLOTTE KYLE MARTIN, *et al.*,
Respondents.

On Petition For Writ Of Certiorari To The Supreme Court of Alabama

MOTION OF THE AMERICAN BANKERS ASSOCIATION FOR LEAVE TO FILE A BRIEF AND BRIEF AS *AMICUS CURIAE* IN SUPPORT OF PETITION

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April 19, 1983

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MOTION OF THE AMERICAN BANKERS ASSOCIATION FOR LEAVE TO FILE BRIEF AS *AMICUS CURIAE* IN SUPPORT OF THE PETITION

To the Honorable, the Chief Justice of the United States and the Associate Justices of the Supreme Court of the United States:

The American Bankers Association respectfully moves, pursuant to Rule 36 of the Rules of this Court, for leave to file the attached brief as *amicus curiae* in support of the petition for a writ of certiorari. The American Bankers Association filed a brief as *amicus curiae* in this case in the Alabama Supreme Court and has sought the consent of the parties to the filing of this brief, but the Respondents have declined to grant that consent.

INTEREST OF THE AMERICAN BANKERS ASSOCIATION

The American Bankers Association is the largest trade association of the commercial banking industry in the United States. It seeks to appear in this case to represent the interests of those of its members now engaged in offering common investment funds to their trust customers, and those of its members who may choose to do so in the future. The decision of the Supreme Court of Alabama in this case resolves issues of federal constitutional law in a manner which, if followed as precedent by other courts, could potentially have an adverse effect upon the trust operations of the banks represented by American Bankers Association nationwide, as more fully set forth in the attached brief.

WHEREFORE, it is respectfully requested that the Court grant the American Bankers Association leave to file the attached brief as *amicus curiae* in support of the petition for a writ of certiorari.

Respectfully submitted,

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QUESTION PRESENTED FOR REVIEW*

Whether the "fluid class recovery" approved by the Alabama Supreme Court in this case deprives the bank or silent class members, or both, of due process of law in violation of the Fourteenth Amendment to the Constitution of the United States.

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*The "Question Presented For Review" in the Petition for Certiorari is stated in broader form, and the Bank's petition deals at length with the notice requirements set forth by this Court in *Mullane* v. *Central Hanover Bank*, 339 U.S. 306 (1950) as well as with the problems of a fluid class recovery. The American Bankers Association supports the Bank's arguments in this respect, but believes that no purpose would be served by our repetition of those arguments.

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AMERICAN BANKERS ASSOCIATION BRIEF AS *AMICUS CURIAE* IN SUPPORT OF THE PETITION

INTEREST OF THE *AMICUS CURIAE*

The American Bankers Association is the largest national trade association of the commercial banking industry in the United States. Its nearly 13,000 members hold in excess of 95% of the assets of all domestic commercial banks. ABA member banks are located in each of the fifty states and the District of Columbia. Over 5,000 commercial banks in the United States have fiduciary powers, and of those, approximately 4,100 actually exercise those powers.[1] Some 1,000 banks operate over 4,800 different

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[1] "Trust Assets of Banks and Trust Companies—1981," Federal Institutions Examination Council, Table A.

common investment funds, consisting of over one million accounts and holding total assets in excess of $115 billion.[2]

A common investment fund is an efficient and productive means of administering small trusts by which the assets of the individual trusts are consolidated into larger funds, achieving economies of scale, diversification, and broader planning than would be possible to accomplish by independent administration of the smaller trusts. This is done, of course, for the benefit of the trust settlors and beneficiaries. In this case, for example, the bank consolidated some 1,250 individual trusts into two common trust funds. Common investment funds are authorized for national banks by regulation of the Comptroller of the Currency. 12 C.F.R. § 9.18 (1982).[3]

When the trustee for a common investment fund makes investment decisions, the performance of the fund affects hundreds or thousands of trusts and their beneficiaries, not just one or a handful. Recognizing that this case may spawn a rash of lawsuits in which the named plaintiffs seek certification as a class action against common investment funds, the American Bankers Association maintains that it is important to the banking industry that some constitutional ground rules be laid down for how or whether such lawsuits are to proceed. Since this case presents the opportunity for the Supreme Court to do so, we respectfully urge the Court to grant the Petition for Writ of Certiorari.

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[2] *Id.*, Table 1, Collective Investment Funds by Classification of Fund.

[3] Common investment funds for national banks are not authorized where such funds would conflict with local law, but that is not an issue in this case.

SUMMARY OF THE ARGUMENT

This Court has earlier specifically reserved judgment, until a later time, on the constitutionality of a "fluid class recovery" in class action lawsuits. Subsequently, two United States Courts of Appeals have held such a procedure unconstitutional. By affirming the trial court decision in this case, the Supreme Court of Alabama has now reached the opposite conclusion, without so much as discussing the issue. Given the conflict among the appellate courts on an important matter of federal constitutional law, we respectfully submit that the time has now come for the Supreme Court to take up and decide the question left open since *Eisen* v. *Carlisle & Jacquelin*, 417 U.S. 156 (1974).

What the *Eisen* case, and the earlier case of *Mullane* v. *Central Hanover Bank*, 339 U.S. 306 (1950) *did* decide was that the requirement of notice to absent class members was of constitutional dimension, not merely a matter of interpretation of procedural rules. By certifying the class in this case under Alabama's version of Rules 23(b)(1) and 23(b)(2) rather than under Rule 23(b)(3), the Alabama courts have improperly attempted to avoid this due process obligation.

ARGUMENT

I. BACKGROUND OF THE CASE

The Bank has long maintained, as sole trustee, two common trust funds, the "Bond Fund" and the "Equity Fund." The investors in these two funds were, in turn, approximately 1,250 individual trusts of which the Bank was either sole trustee or co-trustee. During and after 1971, the Bank's "Bond Fund" invested some of its assets in several Real Estate Investment Trusts. In the mid-1970's, the REIT industry in general fell upon hard times,

and there was a substantial loss in that part of the Bond Fund's investments. The Bank's "Equity Fund" invested its assets in a wide variety of common stocks, some of which also suffered along with the general downturn of the American economy in the mid-1970's. The Respondents filed suit in the Circuit Court of Montgomery County, Alabama, in December, 1978, to recover the losses to the common trust funds, purporting to represent a class consisting of the beneficiaries of the individual trusts which owned participating units in the Bond Fund or the Equity Fund. The Court certified the class on July 26, 1979, and entered Findings of Fact, Conclusions of Law and Judgment in favor of the class on August 19, 1981.

With respect to the lost principal of the Bond Fund, the Bank was

> ordered to forthwith pay into the principal account of the Bond Fund the said sum of $1,226,798.00, . . . recalculate and restate each quarterly valuation of principal . . . (and) promptly distribute to the owners of participating units, including those participating units previously withdrawn, any principal amounts due on the basis of such restated quarterly statements.

(Petition for Writ of Certiorari, App. E., at A-46)

Similar disposition was made of what the Court calculated to have been the income lost to the Bond Fund by reason of the allegedly imprudent investments. (*Id.*, at A-47)

With respect to the lost principal of the Equity Fund, the Bank was ordered to pay into that fund the sum of $1,173,179.03, and distribute that as well to "the owners of the participating units." (*Id.*, at A-49) As above, a similar order was entered directing the Bank to restore lost income of this fund as well to "the owners of participating units." (*Id.*, at A-50)

The "owners of participating units" of the Bond and the Equity Funds are the individual trusts, which were not parties to the lawsuit. The *beneficiaries* of those individual trusts are *not* the owners of participating units, yet these beneficiaries constitute the class certified by the trial court. As we discuss below, this is a crucial distinction, but it is one which was apparently lost on the Alabama Supreme Court.

On appeal, the state Supreme Court affirmed the trial court's decision, but curiously construed the trial court's order as follows:

> In its final order the court ordered the defendant to take whatever actions should be necessary to place the common trust funds *and beneficiaries* in the same position they would have occupied had the bank fully performed its duties.

(Petition for Writ of Certiorari, App. A., at A-13, emphasis supplied.)

In point of fact, the trial court's order did *nothing* directly for the ultimate beneficiaries of the individual trusts. To the extent that the class members benefit at all from the trial court's order, it will be by virtue of those benefits "trickling down" from the individual trusts. Therein lies the source of the constitutional problem in this case.

What the trial court actually did in this case was to decree a "fluid class recovery." Judge Hooper calculated the amount of losses he believed to have been suffered by the common trust funds by reason of the Bank's alleged imprudence, and directed the Bank to disgorge that amount, paying it into the two common trust funds. The common trust funds, in turn, were required to distribute that amount among the participating individual trusts. But that is the end of Judge Hooper's order. What hap-

pens to the money once it is credited to the individual trusts? Obviously, it will be held or distributed in accordance with the terms of the individual trust instruments themselves for *present and future* beneficiaries, not to *past* beneficiaries, although the *past* beneficiaries are the class members who were supposedly harmed by the Bank's alleged imprudence.

Nothing in the trial court's order compels the individual trusts to try to calculate and pay over losses suffered by the actual beneficiaries of the individual trusts from time to time between 1971 and the present, and indeed no such order could very well have been entered. The individual trusts, separate legal entities, were not parties to the lawsuit below. Inevitably, therefore, present and future beneficiaries of the individual trusts will receive the advantages of the Court's order, without regard for whether they have been harmed by the Bank's 1971 investment decisions or not, and in any event in greater degree than any demonstrable losses suffered by them individually.

At the same time, past beneficiaries, who *were* affected by the Bank's investment decisions will receive nothing if the Bank complies with the Court's order. Suppose, for example, that an individual trust had two income beneficiaries for life in 1971, and one of the income beneficiaries died in 1982. The Bank's Common Investment Fund is, by virtue of the Court's order, directed to compensate the individual trust, for *all* of its losses. Should the bank do so in 1983, *all* of the benefit of that order would go to the surviving income beneficiary, even though only half of the total loss was suffered by that survivor. The deceased income beneficiary will have suffered the loss equally, but by reason of the terms of the trust instrument his or her entitlement to any proceeds of the trust ceased before the

trust's losses were restored, and the decedent or his or her estate recovers nothing.

Nor is this a far-fetched or rare example. Over the period of time involved in this case, one's status and interest as beneficiary of a trust can be altered by any number of things: birth, death, divorce, adoption, guardianship, illegitimacy, filiation proceedings, abandonment, inheritance, minority, incompetence, judgments, bankruptcy, attachment, garnishment, and the occurrence or non-occurrence of any number of conditions precedent or conditions subsequent associated with individual trust instruments.

Moreover, even if one assumes that the separate legal entities, the individual trusts, are the members of the class to be compensated for losses (although this would be contrary to the pleadings and allegations in this case), another example shows the presence of a fluid class recovery here as well. Suppose, for instance, that Individual Trust A, with the Bank as sole trustee, purchased for \$100 a common fund unit on January 1, 1972, the day before an alleged imprudent investment. Individual Trust B, having two knowledgeable co-trustees with investment discretion, with full knowledge of the quality of the portfolio, purchased a common fund unit on June 30, 1973 at \$80, a lower price reflecting the drop in value of the "imprudent" investment. Through subsequent appreciation, the value of the common fund unit was \$90 in 1978. Accordingly, Trust A sustained a loss of \$10, whereas Trust B sustained no injury, but on the contrary was advantaged, as the result of the Bank's "imprudent" management. Obviously, the potential rights of Trusts A and B are different, but the trial court's order, affirmed by the State Supreme Court, treats them the same. When the common investment fund replenishes the individual

trusts, the unharmed Individual Trust B receives the benefits of the Court's order at the Bank's expense, as well as Individual Trust A. Neither the Co-Trustees nor the beneficiaries of either trust received any notice or had any opportunity to present any evidence or argument to the trial court about a differentiation among their positions. Due Process was not afforded to the Co-Trustees, the beneficiaries of the Bank.

II. REASONS FOR GRANTING THE PETITION FOR WRIT OF CERTIORARI:

1. This Case Presents An Important Question Of Federal Law Which Has Not Been Decided By The Supreme Court, But Should Be.

In *Eisen* v. *Carlisle & Jacquelin*, 479 F.2d 1005 (2d Cir., 1973), the United States Court of Appeals was faced with a purported class action lawsuit with a class consisting of some six million members. The Court concluded, under the facts of that case, that the suit was unmanageable as a class action unless some sort of "fluid class recovery" was permitted, but that "any such fantastic procedure (is) . . . an unconstitutional violation of the requirement of due process of law." (*Id.* at 1018) This Court reversed the Second Circuit's decision on other grounds:

> (W)e find the notice requirements of Rule 23 to be dispositive of petitioner's attempt to maintain the class action as presently defined. We therefore have no occasion to consider whether the Court of Appeals correctly resolved the issues of manageability and fluid class recovery . . .

Eisen v. *Carlisle & Jacquelin*, 417 U.S. 156, 172, n. 10 (1974)

Nine years after *Eisen*, the "fluid class recovery" issue remains open. This is a particularly appropriate vehicle

for a definitive decision on the constitutionality of a fluid class recovery in class action suits because it differs in at least two significant respects from *Eisen* and similar "fluid class" cases. *Eisen* was an anti-trust and securities law case in which it was claimed that the defendants had profited from their alleged misdeeds. That being the case, there was at least some theoretical justification for compelling the defendants to disgorge any unlawfully received profits so that they would not be unjustly enriched, and such a result could have served to deter any future illegal activities. That is not the case here. In *First Alabama*, the Bank did not profit from its investment decisions. To the contrary, it lost income and fees with the decline in the value of the trust funds along with the individual trusts and their beneficiaries.

Second, other fluid class recovery cases have come about as a result of aggregating many claims which, individually, were too small to warrant litigation by a single aggrieved person. (For example, in *Eisen*, it was calculated that each of the six million class members was entitled to an average of $3.90. *Eisen* v. *Carlisle & Jacquelin, supra.*, 479 F.2d at 1009-1010). Again, there is a theoretical justification in such a case for allowing recovery to "the class as a whole;" otherwise it is likely that *no* actually injured party would recover, and the defendant would escape liability entirely. No such justification is present in this case, since the named plaintiffs claimed to have been injured, personally, in sufficiently substantial amounts that it was worth their while, individually, to pursue their remedies in court. Plaintiff Charlotte Martin claims to have been damaged in the amount of $13,585; Gloria Parker McKeon, $14,536; and Kathleen Gerson "over $10,000.00" (sic). Brief and Argument of Appellees, *First Alabama Bank of Montgomery, N.A.*, v. *Martin*, 425 So.2d 415 (Ala., 1983) at 22.

Thus, the only issue presented here is whether it is constitutional to compensate or over-compensate certain unharmed or minimally harmed class members at the expense of persons who were arguably members of the class at the time of the Bank's challenged investment decisions, but who are no longer class members, where no legitimate goal, policy or object is served thereby.

By affirming the trial court's decision in this case, the Supreme Court of Alabama has held, *sub silentio*, that disparities between the class harmed and the class compensated are acceptable. In doing so, the Court has acted inconsistently with the United States Courts of Appeals of at least two Circuits.

Subsequent to this Court's decision in *Eisen*, the Second Circuit was faced again with the issue of the constitutionality of a "fluid class recovery," and resolved the issue in the same fashion as it had in its *Eisen* opinion:

> We see no reason to change our position, firmly stated in *Eisen* v. *Carlisle & Jaquelin* (sic) 479 F.2d 1005 (2d Cir., 1973, *vacated and remanded on other grounds*, 417 U.S. 156, 94 S.Ct. 2140, 40 L.Ed.2d 732 (1974), disallowing a "fluid class" recovery such as sought by appellants. . . . (T)his method expressly contemplates that silent class members will not receive any compensation, even indirectly. The claims of the silent class members would be expropriated and a windfall might result for those who appeared and collected their share of the damages. Consequently, this procedure might encourage the bringing of class actions likely to result in large uncollected damage pools. It also raises serious questions as to the adequacy of representation where the interests of the named plaintiffs lie in keeping the other class members uninformed. In sum, the defi-

> ciencies of this method of distribution make it a generally unacceptable alternative.

Van Gemert v. *Boeing Co.*, 553 F.2d 812, 815-816 (2d Cir., 1977).

This decision was affirmed by the Supreme Court in *Boeing Co.* v. *Van Gemert*, 444 U.S. 472 (1980), but on grounds having nothing to do with the constitutionality of a fluid class recovery. The Court stated that "as in *Eisen* v. *Carlisle & Jacquelin* . . . we express no opinion on the validity of judgments permitting such recoveries." *Id.* at 480, n. 6 (Citation omitted).

Similarly, the Fourth Circuit has disallowed the use of the fluid class as a means of resolving "the difficulties inherent in proving individual damages" in a class action lawsuit:

> Such a method of computing damages has been appropriately branded as "illegal, inadmissible as a solution of the manageability problems of class actions, and wholly improper."

Windham v. *American Brands, Inc.*, 565 F.2d 59, 72 (4th Cir.) *Cert. denied*, 435 U.S. 968 (1977) (Citation omitted).

We maintain that, in this case as well, compelling the Bank to pay over its funds ultimately to persons whom it has not damaged deprives the Bank of its property without due process of law.

There is another side of the coin as well. Former beneficiaries of the individual trusts will not benefit from the order of the trial court in this case. If they are bound by the doctrine of *res judicata*, as members of the class, then they also have been deprived of their property rights without due process of law. If the former beneficiaries are *not* bound by the court's judgment, and may hereafter bring their own claims against the Bank, then the Bank is

placed at the risk of double liability: having once paid back *all* of the losses incurred to the individual trusts, the Bank may be required to pay damages above and beyond the total losses to those former beneficiaries who are not compensated by the trial court's order. This is not an imaginary concern, for there are circumstances under which the *res judicata* effect of a judgment may be challenged—successfully—by absent class members. See, for example, *Hansberry* v. *Lee*, 311 U.S. 32 (1940).

2. The Supreme Court Of Alabama Has Decided A Question Of Federal Constitutional Law In A Way Which Conflicts With Applicable Decisions Of This Court

It is a fundamental requirement of due process of law, guaranteed by the Fourteenth Amendment, that in any proceeding which is to be accorded finality, notice reasonably calculated to apprise interested parties of the proceeding, and a reasonable opportunity for the interested parties to come forward must be afforded. In the case below, notice was not provided to absent class members, and indeed the Supreme Court of Alabama stated that notice was not required in Rule 23(b)(1) or (b)(2) cases. (Petition for Writ of Certiorari, App. A, at A-14. The reasons why this determination was in error and should be reviewed and reversed by this Court are fully set forth in the Bank's Petition for Certiorari, and no purpose would be served by our repetition of the Bank's arguments, which this *amicus* entirely supports. We mention it again here solely to emphasize the importance of the issue. This is not simply a matter of a state court construing its own rules of procedure. Rather, it is an authoritative decision, by a court of last resort, construing a rule shared, for all intents and purposes, by the federal court system and the courts of thirty-two states and the District of Columbia. (Petition for Writ of Cer-

tiorari, at 17.) Moreover, the Alabama courts have construed their procedural rules in a fashion implicating important Federal constitutional guarantees, to the detriment of the Petitioner, absent class members, and untold future litigants who must face the adverse precedent established in this case.

CONCLUSION

For the reasons stated above, the American Bankers Association respectfully maintains that where fundamental issues of federal due process of law rights are involved, as here, the outcome of the case ought not depend upon where the case is tried. The Alabama courts have ruled on the issues inconsistently with the decisions of two United States Courts of Appeals, and with decisions of this Court leaving it to this Court, and this Court alone, to resolve the discrepancy. The Petition for Writ of Certiorari should be granted.

Respectfully submitted,

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